SUPREME COURT, U. S.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1962

No. 208

COMPTROLLER OF THE TREASURY OF THE STATE OF MARYLAND, RETAIL SALES TAX DIVISION,

Petitioner,

v.

PITTSBURGH-DES MOINES STEEL COMPANY,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

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NO. _____

COMPTROLLER OF THE TREASURY OF THE STATE OF MARYLAND, RETAIL SALES TAX DIVISION,

Petitioner,

v.

PITTSBURGH-DES MOINES STEEL COMPANY,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

Petitioner prays that a Writ of Certiorari issue to review the judgment of the Court of Appeals of Maryland entered in the above entitled case on March 19, 1963.

CITATIONS TO OPINION BELOW

The opinion of the Court of Appeals of Maryland is reported in 231 Md. 132, and in 189 A. 2d 107. It is printed in Appendix B hereto, *infra*, page 3a.

JURISDICTION

The judgment of the Court of Appeals was entered on March 19, 1963. There was no motion for reargument. The jurisdiction of this Court is invoked under 28 U.S.C.A. 1257(3).

QUESTIONS PRESENTED

1. Is there a reasonable ground for a distinction between contractors dealing with the Federal Government and contractors dealing with the State of Maryland, its political subdivisions, and charitable, educational and religious institutions?

2. Does the fact that the State of Maryland exempts from sales tax certain sales to contractors who contract with the State of Maryland and its political subdivisions while taxing sales to contractors who contract with the Federal Government, result in discrimination against contractors with the Federal Government?

3. If there is discrimination against contractors with the Federal Government, is such discrimination justified and therefore not in violation of the Constitution of the United States?

STATUTES AND RULES INVOLVED

The statutory provisions directly involved are Section 324(f)(3), Section 325, Section 326(a), Section 326(f) and Section 326(i) of Article 81 of the Annotated Code of Maryland (1957 Edition). Rule 70 of the Rules of the Comptroller of the Treasury of the State of Maryland under the Retail Sales and Use Tax Acts is also involved. The statutes involved and the rule are printed in Appendix A, *infra*, page 1a.

STATEMENT OF THE CASE

On April 6, 1961, the Comptroller of the Treasury of the State of Maryland made an assessment for sales and use taxes against Pittsburgh-Des Moines Steel Company in the amount of $20,389.83. Of this assessment $17,980.65 represented tax on materials incorporated into a bridge con-

structed by Pittsburgh-Des Moines Steel Company under a lump sum contract with the Department of Commerce of the United States, and this amount is the only part of the assessment involved in the instant petition. Pittsburgh-Des Moines Steel Company contended that the assessment was unconstitutional since the State of Maryland did not tax materials incorporated into projects constructed for the State of Maryland, any of its political subdivisions or any charitable, religious or educational organizations. The Comptroller contended that, since the State had to pay all the costs of its own contracts and had to supply a large part of the revenue of each political subdivision, there was a valid reason for the distinction, which did not discriminate, or, at the very least, there was justification for the State seeking not to increase the cost of its contracts and the contracts of its political subdivisions. All of the increased costs could only be recovered from additional tax revenues. A formal hearing was held before a Hearing Officer, who sustained the assessment.

Pittsburgh-Des Moines Steel Company appealed to the Circuit Court of Anne Arundel County and again contended that, since the State of Maryland did not tax contractors who contracted with the State, or any of its political subdivisions, or charitable, religious or educational organizations on materials incorporated into projects constructed for the State, any of its political subdivisions, or any charitable, religious or educational organizations, the tax on a contractor who contracted with the Federal Government on materials incorporated into a project constructed for the Federal Government created an unconstitutional discrimination against contractors for the Federal Government. The Comptroller again illustrated that if the State taxed contractors who dealt with the State and its political subdivisions, the taxes of all taxpayers, including contrac-

tors dealing with the Federal Government, would increase and that the classification was reasonable and there was no unjustified discrimination. The Comptroller showed that over one-half of all tax moneys collected by the State was returned by the State to the political subdivisions. The Circuit Court for Anne Arundel County (O. Bowie Duckett, Judge) held that the assessment did unconstitutionally discriminate against Pittsburgh-Des Moines Steel Company and declared the assessment invalid and abated.

From that decision, the Comptroller appealed to the Court of Appeals of Maryland. That court, which is the highest court of Maryland, and which had proper jurisdiction of the matter on appeal from the lower court, on March 19, 1963, affirmed the decision of the lower court. In its opinion, the court held that there was discrimination, there was no reasonable basis for the discrimination and, therefore, the tax assessed was invalid and void as being an unconstitutional discrimination against contractors dealing with the Federal Government. The court indicated that Maryland could tax contractors dealing with the Federal Government if the law was changed so that persons contracting with the State or any of its political subdivisions would also be subject to the tax.

REASONS FOR GRANTING THE WRIT

I. THE DECISION OF THE COURT OF APPEALS OF MARYLAND FINDS A TAX IMPOSED BY THE STATE OF MARYLAND TO BE IN VIOLATION OF THE CONSTITUTION OF THE UNITED STATES CONTRARY TO THE DECISIONS OF THIS COURT IN SEVERAL CASES INCLUDING THE CASE OF *UNITED STATES v. CITY OF DETROIT*.

In the case of *United States v. City of Detroit*, 355 U.S. 466, 78 S. Ct. 474, 2 L. Ed. 2d 424 (1958), this Court sustained the constitutionality of a Michigan statute which provided that when tax exempt real property is used by a

private party in a business conducted for profit, the private party is subject to taxation to the same extent as though he owned the property, even though the statute granted an exemption to such private parties who used the real property of any state-supported educational institution. In that situation the persons who used the property of the Federal Government clearly were not treated in the same manner as persons who used the property of educational institutions supported by the State of Michigan. The full text of the statutory provision involved was set forth in the decision of the Supreme Court of Michigan, which was affirmed by this Court, *United States v. City of Detroit*, 345 Mich. 601, 77 N.W. 2d 79 (1956); as follows:

> "Sec. 1. When any real property which for any reason is exempt from taxation is leased, loaned or otherwise made available to and used by a private individual, association or corporation in connection with a business conducted for profit, except where the use is by way of a concession in or relative to the use of a public airport, park, market, fair ground or similar property which is available to the use of the general public, shall be subject to taxation in the same amount and to the same extent as though the lessee or user were the owner of such property: Provided, however, That the foregoing shall not apply to federal property for which payments are made in lieu of taxes in amounts equivalent to taxes which might otherwise be lawfully assessed *or property of any state-supported educational institution.*" (Emphasis supplied.)

A thorough reading of the *United States v. City of Detroit* case with the complete statutory provision in mind shows that that case cannot be reconciled with the decision of the Court of Appeals of Maryland in the instant case. It is true that in the case of *Phillips Chemical Company v. Dumas Independent School District*, 361 U.S. 376, 80 S. Ct. 474, 4 L. Ed. 2d 384 (1960), this Court indicated that neither

the government nor its lessees in the Michigan case claimed that the exemption of lessees of property owned by educational institutions supported by the State of Michigan discriminated against them. However, there can be no question that the exemption was in the statute and that it did result in lessees from the Federal Government paying taxes which lessees from educational institutions supported by the State of Michigan did not have to pay.

In addition, this Court, recently, without opinion, affirmed a decision of a 3-judge District Court in the case of *United States v. Department of Revenue of the State of Illinois*, 202 F. Supp. 757 (N.D., Ill., 1962), *affirmed, per curiam*, 371 U.S. 21, 83 S. Ct. 117, 9 L. Ed. 2d 95, which held that an exemption for retailers dealing with non-government institutions operated for charitable, religious or educational purposes did not discriminate against retailers dealing with the Federal Government.

While the above case was cited by the Court of Appeals of Maryland to support its conclusion in the instant case, the language of the opinion of the 3-judge District Court with regard to the exemption for retailers dealing with charitable, religious and educational institutions indicates that it is really a continuation of the doctrine set down in *United States v. City of Detroit, supra.* The court held that there was a reasonable basis for classification and exemption, since:

> "The exemption of these institutions encourages their existence and relieves the State of the heavy burden of maintaining and performing these essential services." 202 F. Supp. 757, at 759.

This decision also illustrates the holding in the *Phillips Chemical Company v. Dumas Independent School District* case, *supra*, that discrimination itself is not unconstitutional but unjustified discrimination is unconstitutional.

The State of Maryland did not attempt to make matters more difficult for contractors dealing with the Federal Government. It merely determined that a certain amount of tax revenue was necessary to perform its functions as a state. If the State of Maryland were to place a tax on contractors doing business with the State and with its political subdivisions, as suggested by the Maryland Court of Appeals, in order to be able to tax contractors dealing with the Federal Government, the cost to the State for its contracts would increase and additional tax revenue would be needed. Contractors with the Federal Government would be in no better position than they are under the law as it now exists since all taxpayers would be required to pay higher taxes in order to reimburse the State for the additional cost of its contracts. The higher tax would be magnified by the fact that there would be costs in collecting the tax from contractors with the State and with the political subdivisions that would also have to be paid from the tax revenues. These factors were brought out in this case but were rejected by the Maryland Court of Appeals. Petitioner contends that these factors are as much a justification for any so-called discrimination as the justification for the exemption for State-supported educational institutions involved in *United States v. City of Detroit, supra*, and the exemption for charitable, religious and educational institutions in *United States v. Department of Revenue of the State of Illinois, supra*. If the State can enhance its own position indirectly by exempting persons dealing with charitable, religious and educational institutions, it should also be able to enhance its own position directly by exempting persons dealing with the State and its political subdivisions.

The exemption of contractors dealing with the political subdivisions decreases the cost of operation of the political

subdivisions and "relieves the State of the heavy burden of maintaining and performing" the many services maintained and performed by the political subdivisions. In addition, the lower the cost to the State of its contracts, the lower the tax burden that the State will have to impose on all of its taxpayers, including contractors dealing with the Federal Government.

Petitioner therefore contends that the decision of the Court of Appeals of Maryland in the instant case is contrary to the decision of this Court in *United States v. City of Detroit, supra*, and to the specific language of the decision of the 3-judge District Court in *United States v. Department of Revenue of the State of Illinois*, 202 F. Supp. 757; *supra*, affirmed by this Court without opinion.

II. THE DECISION OF THE COURT OF APPEALS OF MARYLAND FINDS A TAX IMPOSED BY THE STATE OF MARYLAND TO BE IN VIOLATION OF THE CONSTITUTION OF THE UNITED STATES FOR REASONS WHICH INDICATE THAT THERE IS A MISCONCEPTION ARISING OUT OF CERTAIN DECISIONS OF THIS COURT.

The case of *McCulloch v. Maryland*, 4 Wheaton 316, 4 L. Ed. 579, was the first case to hold that while there was no express provision in the Constitution of the United States to prohibit states from taxing the Federal Government and its instrumentalities, such a provision was inherent within the four corners of the Constitution of the United States. A great many cases of this Court, including *James v. Dravo Contracting Co.*, 302 U.S. 134, 58 S. Ct. 208 (1937); *Alabama v. King & Boozer*, 314 U.S. 1, 62 S. Ct. 43 (1941); and *Curry v. United States*, 314 U.S. 14, 62 S. Ct. 48 (1941), are the basis for the accepted principle that the constitutionality of a state tax is related to the incidence of the tax and that even though the economic burden of the tax might fall directly on the government or its agency, the tax would not be unconstitutional on that basis. The case

of *United States v. City of Detroit, supra*, is but a manifest extension of the three cases cited above.

The concept that a tax which is imposed directly on the Federal Government may be unconstitutional if it discriminates was most forcibly stated in the *Phillips Chemical Company v. Dumas Independent School District* case, *supra*, which indicates that even where there is discrimination, if the discrimination can be justified, the tax would be constitutional. This Court found that the reasons advanced by the state in the *Phillips* case, as justifying the distinction, simply did not exist. The *Phillips* case indicates that the state should treat those who deal with the Federal Government as well as those with whom it deals itself. However, it is impossible for a state to treat the Federal Government as well as it treats itself in tax matters for, even if the state, in effect, collects from itself as well as from the Federal Government, the state is just transferring money from one pocket to another and is not required to divide any of it with the Federal Government.

The case of *Moses Lake Homes, Inc. v. Grant County*, 365 U.S. 744, 81 S. Ct. 870, 6 L. Ed. 2d 66, and the case of *United States v. Department of Revenue of the State of Illinois*, 191 F. Supp. 723 (N.D., Ill., 1961), *judgment vacated* 368 U.S. 30, 82 S. Ct. 146, 7 L. Ed. 2d 90, find the *Phillips* case to be controlling. In the Illinois case the court indicated that there was discrimination and that there was no attempt by the State of Illinois to justify the discrimination. Subsequently, the State of Illinois amended its law to provide that retailers dealing with the state would pay the same tax as paid by retailers dealing with the Federal Government, but Illinois retained an exemption for retailers dealing with religious, educational and charitable institutions. The tax was then held to be constitutional in *United States v. Department of Revenue of the State of Illinois*, 202 F. Supp. 757, *supra*.

The Court of Appeals of Maryland felt that the above decisions of this Court require the Court of Appeals to give no weight to the argument of the Comptroller of the Treasury of the State of Maryland concerning the reasons for taxing contractors dealing with the Federal Government and not taxing contractors dealing with the State or its political subdivisions. The Comptroller proved that there was a valid reason for the different classifications or, in the very minimum, proved that there was a valid justification for any discrimination against contractors dealing with the Federal Government and, therefore, the tax as applied should have been found to be constitutional.

If this Court does not grant the Writ of Certiorari, all states will be faced with another decision which further limits their sources of revenue and the states will not have the benefit of a decision of this Court as to what constitutes a reasonable classification in this area of taxation and what are the standards to determine if there is reasonable justification for any discrimination against persons dealing with the Federal Government.

Therefore, Petitioner contends that this Court should grant the Writ of Certiorari to determine whether or not the Court of Appeals of Maryland was correct in determining that there was no justification for any alleged discrimination and that therefore the tax violated the Constitution of the United States.

III. THIS CASE PRESENTS A FEDERAL QUESTION OF SUBSTANCE WHICH IS AN EXTENSION OF AND GOES FURTHER THAN ANY PREVIOUS DECISIONS OF THIS COURT AND IS A MATTER WHICH SHOULD BE DECIDED BY THIS COURT.

The question of what constitutes a reasonable classification under a tax statute which imposes a tax on all contractors with private individuals, all contractors with the Federal Government and all contractors with other states

and the District of Columbia but exempts all contractors with the State of Maryland and its political subdivisions has not been squarely decided by this Court as yet. Nor has this Court decided the question as to what would be reasonable grounds to justify a state, by statute, to purport to discriminate against certain taxpayers dealing with the Federal Government in order to avoid having to collect taxes from its contractors with one hand and then pay out the very same money with the other hand to pay for the increase in price of the necessary contracts of the state.

There is no question that in recent years the states and their political subdivisions have been faced with serious problems of finding sources of tax revenues to pay for necessary functions of the states and their political subdivisions. The decision of the Court of Appeals of Maryland, if not reviewed by this Court, will in all probability be used by many other courts to deny to the states certain tax revenues which for many years were paid to the states without question. Many states are already faced with a problem of whether or not to amend their present tax statutes and how to do so in view of the affirmance by this Court, without opinion, of the decision of the 3-judge District Court in *United States v. Department of Revenue of the State of Illinois*, 202 F. Supp. 757, *supra*. The case indicates that a state can tax persons dealing with the Federal Government if it also taxes persons dealing with the state and its political subdivisions, even though it does not tax persons dealing with charitable, religious and educational institutions.

This decision was made in spite of the fact that it can be shown, and was shown in the instant case, that such a tax results in the state collecting money from persons dealing with the state or its political subdivisions and then paying out the same money plus probable additional profits

to the persons dealing with the state and its political subdivisions in the form of higher contract prices. Requiring the state to comply with the legal fiction of collecting a tax from itself in order to be able to tax persons dealing with the Federal Government will not in the long run decrease the costs which will be passed on by contractors to the Federal Government. It merely provides a windfall to those contractors who now find that they do not have to pay a tax they always contemplated paying or that they are entitled to a refund of a tax they have paid in the past.

Once the states change their laws so as not to "discriminate", the contractors with the Federal Government and the other citizens of the state will pay the same taxes they would have paid in any event. In addition, they will be required to make up to the state the additional cost imposed upon the state in requiring the state to collect a tax, in effect, from itself, which can only increase its costs of operation.

This precise point of whether or not the attempts by the state to avoid a costly legal fiction in its taxation program constitute reasonable ground for a classification exempting persons dealing with the state and its political subdivisions from a tax otherwise applied generally has not been decided by this Court. In the instant case the facts are undisputed and this precise question can be reviewed on a record that is quite clear. A decision can be made which will serve the Federal Government and all of the states in that it will answer the one question remaining unanswered with regard to the ability of the states to tax persons dealing with the Federal Government.

It has been shown that a comparison of the case of *United States v. City of Detroit, supra,* with the case of *Phillips Chemical Company v. Dumas Independent School*

District, supra, and the case of *United States v. Department of Revenue of the State of Illinois*, 202 F. Supp. 757, *supra*, *affirmed per curiam*, 371 U.S. 21, 83 S. Ct. 117, leaves the exact status of the law as to reasonable classification and justifiable discrimination less than settled.

A decision by this Court to grant the Writ of Certiorari and to review this case would enable this Court to tie together the loose ends and to settle the questions left unsettled by the cases cited above.

CONCLUSION

For the foregoing reasons, this Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX A

STATUTORY PROVISIONS AND RULE INVOLVED

ANNOTATED CODE OF MARYLAND (1957 EDITION) ARTICLE 81

§324. Definitions.

As used in this subtitle, the following terms shall mean or include:

(f) "Retail sale" and "sale at retail" shall mean the sale in any quantity or quantities of any tangible personal property or service taxable under the terms of this subtitle. Said term shall mean all sales of tangible personal property to any person for any purpose other than those in which the purpose of the purchaser is to resell the property so transferred in the form in which the same is, or is to be received by him, or to use or incorporate the property so transferred, as a material or part, of other tangible personal property to be produced for sale by manufacturing, assembling, processing or refining. For the purpose of the tax imposed by this subtitle, the term "sale at retail" shall include but shall not be limited to the following:

(3) The sale of tangible personal property to contractors, builders or landowners for use or resale in the form of real estate.

§325. Rate of tax.

For the privilege of selling certain tangible personal property at retail as defined above and for the privilege of dispensing certain selected services defined as sales at retail by §324 (f) of this subtitle, a vendor shall collect from the purchaser a tax at the rate specified in this section on the price of each separate retail sale made in this State on or after the date of this act. The tax imposed by this section shall be paid by the purchaser and shall be computed subject to the terms and conditions of §334 of this subtitle as follows:

* * * * * * *

§326. Exemptions.

The tax hereby levied shall not apply to the following sales:

(a) *State sales.* — Sales to the State of Maryland or any of its political subdivisions.

(f) *Tax prohibited by United States Constitution.* — Sales which are not within the taxing power of this State under the Constitution of the United States.

(i) *Sales to nonprofit, charitable, etc., organizations.* — Sales to any person operating a nonprofit religious, charitable, scientific, literary or educational institution or organization situated in this State when such tangible personal property is purchased for use in carrying on the work of such institution or organization; provided that the word "person," as used in this subsection shall not include the United States of America or any agency or instrumentality thereof.

RULE 70 OF THE RULES OF THE COMPTROLLER OF THE TREASURY OF THE STATE OF MARYLAND UNDER THE RETAIL SALES AND USE TAX ACT

Rule 70:

Sales to Contractors Performing Jobs for Certain Exempt Persons

Contractors who are performing jobs for the State of Maryland or any of its political sub-divisions or a non-profit religious, charitable, scientific, literary or educational institution or organization located within the State of Maryland on a lump-sum basis are not required to pay the tax on materials and supplies which will be incorporated into the job. No exemption certificates will be issued by the Comptroller to cover such purchases. The contractor shall present to his supplier the contract designation or number as his authority for making tax-free purchases of materials and supplies to complete such contracts.

The contractor must pay the tax on all equipment which he purchases even though it may be used on a job for one of the aforementioned persons.

Contractors who are working on lump-sum, cost plus a fixed fee, or cost plus contracts containing an upset or guarantee clause with the Federal Government must pay

the tax on all personal property which they purchase in fulfilling such contracts.

APPENDIX B

Opinion of Court of Appeals of Maryland

(Filed March 19, 1963)

Prescott, J.:

In April, 1961, the Comptroller of the Treasury, the appellant and cross-appellee (often hereafter referred to as the appellant), made an assessment, for the period June 1, 1960, through January 30, 1961, for sales taxes against Pittsburgh-Des Moines Steel Company, the appellee and cross-appellant, (often hereafter referred to as the appellee) of $17,980.65, representing tax on materials incorporated into the Woodrow Wilson Memorial Bridge, constructed by Pittsburgh under a lump-sum contract with the Department of Commerce of the United States Government. In addition, an assessment of $2,409.18 was imposed on rentals of floating equipment used by Pittsburgh in the construction of the bridge. Following a formal hearing before the Comptroller, the hearing officer sustained the entire assessment. An appeal was taken by Pittsburgh to the Circuit Court for Anne Arundel County, where Judge Duckett abated the assessment against the materials, but sustained the assessment on rentals. Both parties appealed.

The appeal presents four questions:

1. Does Rule 70 of the sales tax rules and regulations discriminate against the appellee by exempting certain sales to contractors with the State of Maryland and its political subdivisions while taxing sales to federal contractors?

2. If Rule 70 discriminates against the appellee, is such discrimination unconstitutional?

3. If the Court finds there is unconstitutional discrimination against the appellee, what is the result?

4. Does the Maryland sales tax apply to rentals of tangible personal property?

The facts are few and undisputed: assessments were made against Pittsburgh as above noted, and, during the time of the construction of the bridge involved, Maryland did not assess a sales or use tax on materials which were incorporated into "jobs" under contracts with the State of Maryland, or its political subdivisions.

I.

The appellant argues that under the facts of this case, there has been *no* discrimination against Pittsburgh. He asserts that the sales tax has been imposed by statute (Code, 1962, Cum. Supp., Art. 81, §324, (f) (4), and §325) on the sale to all contractors of tangible personal property to be used in constructing real estate; hence contractors with "the Federal Government are, of course, included and contractors for the State are also included except for the provisions of Rule 70."

The latter part of the above quotation cannot be sustained. The Comptroller has no power or authority to create an exemption by Rule. Rule 70 derives whatever force it has from the fact that it is a correct interpretation of the statutes promulgated by the Legislature. Article 81, §326 (a), exempts from the sales tax "sales to the State of Maryland or any of its political subdivisions." In *John McShain, Inc.* v. *Comptroller*, 202 Md. 68, 95 A. 2d 473, wherein it was conceded that the Comptroller lacked the

"Contractors who are performing jobs for the State of Maryland or any of its political sub-divisions or a nonprofit religious, charitable, scientific, literary or educational institution or organization located within the State of Maryland on a lump-sum basis are not required to pay the tax on materials and supplies which will be incorporated into the job. * * *

"Contractors who are working on lump-sum, cost plus a fixed fee or cost plus contracts containing an upset or guarantee clause with the Federal Government must pay the tax on all personal property which they purchase in fulfilling such contracts."

power to create an exemption beyond that granted by statute) this Court upheld a part of Rule 70 (as it now reads), and held that the exemption applied when the tangible personal property was acquired through an intermediary contractor, as well as when it was acquired directly from a supplier. Cf. *Comptroller v. Joseph F. Hughes*, 209 Md. 141, 120 A. 2d 343. Hence, we see that the exemption of sales to the State of Maryland and its political subdivisions stems from Article 81, §326 (a), and the exemption in Rule 70 to contractors who are performing jobs for the State or its political subdivisions has been confirmed by this Court as a proper interpretation of the exemptions created by statute.

It is impossible, under the adjudicated cases, to sustain the Comptroller's claim that the record discloses *no* discrimination against the appellee as a contractor with the Federal Government. In *Phillips Chemical Co. v. Dumas School Dist.*, 361 U.S. 376, the State of Texas had imposed a tax upon lessees of tax-exempt real estate owned by the Federal Government. This tax was measured by the full value of the property. However, by Texas law a distinctly lesser burden was placed upon the lessees of tax-exempt property owned by the State, or its political subdivisions. Under these circumstances, the Supreme Court stated: "The discrimination against the United States and its lessee seems apparent."

In 1961, the Supreme Court again had occasion to consider the question of discrimination against the United States and its lessees. In *Moses Lake Homes v. Grant County*, 365 U.S. 744, Grant County, pursuant to the laws of the State of Washington, attempted to tax the full value of the buildings and improvements on privately owned Wherry Act leaseholds of housing developments on a federally owned Air Force base, although, under the laws of Washington, other leaseholds, including privately owned leaseholds of tax-exempt State lands, were taxed at a lower valuation. The Court quoted from *United States v. City of Detroit* (355 U.S. at 473) as follows: "It still remains true, as it has from the beginning, that a tax may be invalid

even though it does not fall directly on the United States if it operates so as to discriminate against the Government or those with whom it deals." It then followed the *Phillips Chemical Co.* case, *supra*, and held the tax to be unconstitutional and void, because it discriminated against the United States and its lessees.

These two cases dealt with "property" taxes, but it has been held that the principles there involved are equally applicable in the case of sales taxes. The State of Illinois imposed a retailer's occupation tax—a tax on the seller's privilege to sell tangible personal property at retail based on the amount of the sales price—upon the vendors of tangible personal property. An exemption was granted to vendors to the State and its political subdivisions, but no such exemption was afforded vendors to the Federal Government.

In *United States and Olin Mathieson Chemical Corp. v. Dep't of Revenue of State of Illinois*, 191 F. Supp. 723 (1961) (D.C., N.D. Ill.), a three-judge Federal Court stated that in its view a retailer who deals with the Federal Government falls within the same class as a retailer who deals with the State of Illinois, and it was very difficult to perceive a reasonable distinction which grants the State freedom from contributing to the cost of government and imposes the burden on the Federal Government. It then pointed out that the imposition of the tax on one and not the other permitted the State to deal with retailers at a lower cost and imposed an increased cost upon the Federal Government dealing with the same class of persons. The tax was held to be unconstitutional and void as discriminating against the Federal Government, or those with whom it dealt. The State of Illinois appealed to the Supreme Court.

While this appeal was pending, the Supreme Court of Illinois found the exemption section of the occupation tax law to be unconstitutional. Thereafter, the General Assembly of Illinois enacted an exemption section, which did not exempt the tax on sales to the State or its political subdivisions, but did exempt charitable institutions. The

Supreme Court vacated the judgment "in the light of developments which have occurred," and remanded the case for further consideration. 368 U.S. 39. On remand, the case was tried on the issue of whether the exemption of charitable institutions created an unconstitutional discrimination. The Court determined that it did not, but issued an injunction restraining the collection of taxes on the proceeds of sales to the Government "for the period when the State of Illinois did not assess or collect any taxes with respect to proceeds of sales to the State of Illinois," or its political subdivisions. This determination was affirmed by the Supreme Court. *United States v. Dep't of Revenue*, 371 U.S. 21. The three-judge Federal Court was correct we think, in determining that the same principles enunciated in *Phillips Chemical Co.* and *Moses Lake Homes, Inc.* were applicable to sales taxes, and we hold that the record discloses discrimination against the Federal Government and those with whom it dealt. See also *People v. Isaacs*, 176 N.E. 2d 889 (Ill. 1961).

II.

The appellant's next contention is that assuming the law does discriminate against the appellee, such discrimination is not unconstitutional, because there is "a reasonable basis for treating state contractors as one class and federal contractors as another."

At the outset of the consideration of this contention, we note that there seems to be a considerable difference of opinion in the briefs as to the tests or standards to be applied in determining what, or how much, discrimination by a State against the Federal Government, or those with whom it deals, is necessary to render such discrimination unconstitutional.

The brief of the United States, as *amicus curiae*, argues that the classifications and discriminations permissible under the Equal Protection Clause have nothing whatever to do with the problems herein involved, claiming that they should be solved solely by reference to the Supremacy Clause of the United States Constitution. It points to the fact that the seminal case upon the subject, *McCulloch v.*

Maryland, 4 Wheat. 316, was decided fifty years before the Fourteenth Amendment was adopted. It quotes from *Phillips Chemical Co.*, *supra*, wherein the Court said: "We have made it clear, in the equal protection cases, that our decisions in that field are not necessarily controlling where problems of intergovernmental tax immunity are involved. * * * But where taxation of the private use of the Government's property is concerned, the Government's interests must be weighed in the balance," and from the opinion in *United States v. Allegheny County*, 322 U.S. 174, 191, to the following effect: "The questions in this case [taxation by a State of property owned by the Federal Government, in the custody of its bailee] do not arise under the Fourteenth Amendment. They depend on provisions adopted and principles settled long before the Fourteenth Amendment and which exist independently of it." It also cites *Martin v. State Tax Commission*, 225 Md. 404, 421, 171 A. 2d 479, where Chief Judge Brune, for the Court, said: "In view of the conclusion which we have reached [on the facts of the case] we do not find it necessary to express an opinion on the question of possible discrimination against the Government on the basis of either statutory provisions or actual tax administration. Of course, no such discrimination would be permissible." Consequently, the *amicus curiae* concludes that *any* State tax "levied in a discriminatory manner against those who deal with the Federal Government is prohibited and invalid."

The Comptroller counters by claiming that the tests of discrimination used in the equal protection cases are applicable here; that the last clause of Article 15 of the Declaration of Rights ["yet fines, duties or taxes may properly and justly be imposed, or laid with a political view for the good government and benefit of the community"] permits a higher degree of discrimination in imposing excise taxes than in imposing property taxes; that in the *Phillips Chemical Co.* and *Moses Lake Homes, Inc.* cases, *supra*, there is no discussion (with the possible exception of *Phillips*) "of what might constitute discrimination"; and in *Phillips Chemical Co.*, the Court, after pointing out that discrimination against the United States and its lessees

was apparent, stated: "the question, however, is whether it can be justified," which can only mean that even if there be admitted discrimination, the statute creating the discrimination is not unconstitutional if the discrimination can be justified.

We find it unnecessary to answer these contentions in detail, or to lay down a rule relative to the tests and standards to be applied in all cases where it is claimed that a State tax discriminates against the Federal Government and those with whom it deals. For the purposes of this case, we shall adopt the simple test set forth by the Supreme Court in *Phillips Chemical Co., supra*, when it said: "The imposition of a heavier tax burden on lessees of federal property than is imposed on lessees of other exempt public property must be justified by significant differences between the two classes. * * *. * * * where taxation of the private use of the Government's property is concerned, the Government's interests must be weighed in the balance. *Accordingly, it does not seem too much to require that the State treat those who deal with the Government as well as it treats those with whom it deals itself* (italics ours)."

The appellant argues this contention (No. II) elaborately, but an analysis of his brief discloses the following is the claimed "reasonable basis" for placing state and federal contractors in different classes: "In the case at bar, the distinctions are quite evident. The exemption of State contractors does not increase the burden on anyone else. As a matter of fact, it lessens the burden on all since it is perfectly obvious that there are expenses attendant upon the handling of any tax funds * * *. The direct benefit to the State and its political subdivisions is so amply revealed in the State's budget, that it is not necessary to discuss it here. Rule 70 does not set up a classification based on sovereignty but is merely a common sense application of the fact that there can be no profit in paying the right hand with the left. * * *. The point we [the Comptroller] make is that the exemption for State contractors does not increase the tax burden of other contractors or taxpayers but decreases the tax burden on all."

We do not find the argument persuasive. The argument that the exemption lessens the burden on the State because "there are expenses" incurred in the collection and handling of tax funds and that there is a "direct benefit" to the State and its subdivisions applies with equal force when the Federal Government is considered, and it weakens, more than it strengthens, the appellant's position. And practically all, if not all, of the above argument has been answered adversely to the Comptroller in the cases we have cited, above. We are unable to discover "significant differences" between contractors with the Federal Government and contractors with the State of Maryland, or its political subdivisions — the classes erected by our sales tax law. A contractor who deals with the Federal Government falls, we think, within the same class as a contractor with the State of Maryland, or its subdivisions. Where the State creates an exemption[2] from the general classification of sales to contractors who purchase tangible personal property for the construction of real estate on the legally supportable basis of contracting with the State of Maryland, it is because such contractor deals with a governmental entity. When the sales tax law exempted contractors who deal with the State and its subdivisions, but failed to exempt contractors who deal with the Federal Government, the Legislature subdivided contractors with governmental entities into, at least, two divisions: those who contract with the State and its subdivisions and those who contract with the United States. Such an exemption, to be legally justifiable, must fall alike on all who are similarly situated and must include contractors with the Federal Government. *United States v. Dep't of Revenue of State of Illinois, supra.* Cf. *Phillips Chemical Co. v. Dumas School Dist.* and

[2] No attack is made in the instant case on the power of the State to create an exemption. But statutes which tax one class while exempting another class necessarily impose a greater burden upon the person taxed than would be the case if the exempted class were included. However, such statutes do not create a constitutional inequality, if all who should be included in the same class are included and treated alike. United States v. Dep't of Revenue of State of Illinois, supra; Hart Refineries v. Harmon, 278 U.S. 499, 502.

Moses Lake Homes, Inc. v. Grant County, both *supra*. We agree with the three-judge Federal Court when (191 F. Supp. at p. 729) it said:

> "It is difficult for us to perceive a reasonable distinction which grants one freedom from contributing to the cost of government and imposes the burden upon the other. Further, the imposition of the tax upon one and not the other permits the State to deal with retailers at a lower cost and imposes an increased cost upon the Federal Government dealing with the same class of persons. Assuming that the statutory exemption may have the laudable public purpose of reducing governmental costs, it is equally applicable to the Federal Government thus benefiting all citizens of the United States, including the citizens of the State of Illinois."

See also *United States v. City of Detroit*, *supra*, 355 U.S. at p. 474.

The above answers substantially all of the appellant's argument under this heading. However, there is one further claim which we shall answer. The Comptroller states that, beginning in 1947 when the sales tax was first imposed in Maryland, the General Assembly adopted a plan whereby the State paid over to its political subdivisions certain taxes, collected by the State, to enable the subdivisions to meet "their deferred building requirements and other expenditures required by the Second World War * * *" and the sales and use tax laws were adopted "to fill the gap occasioned by the payment" of the aforementioned funds to the political subdivisions. There is nothing in the record to show that the sales tax is earmarked or allocated for any specific purpose, and, presumably, it goes into the general funds of the State. But be that as it may, we think the short, but complete, answer to this claim is, that no matter for what purpose the State of Maryland imposes its sales tax, it does not justify the State in discriminating, individually, against the Federal Government.

We, therefore, hold that the record fails to show "significant differences" between contractors with the Federal

Government and contractors with the State and its subdivisions; and when the Legislature enacted Article 81, §326 (a), which exempted sales to the State and its political subdivisions but did not exempt sales to the Federal Government, it failed to "treat those who deal with the Government as well as it treats those with whom it deals itself." Hence, the tax assessed against Pittsburgh for the sales on tangible personal property incorporated into the bridge is invalid and void, and cannot lawfully be collected.

III.

The appellant suggests under this heading that if this Court finds an unjustifiable discrimination, the proper way of removing such discrimination "is by striking down Rule 70,[3] the true source of any discrimination which may exist," and then state and federal contractors will be taxed alike. As we pointed out above, the true source of the exemption to contractors who deal with the State and its subdivisions is Article 81, §326 (a). Hence, if Rule 70 were stricken down, Article 81, §326 (a) would remain in force and effect, and the discrimination would still exist.

We think that instead of striking down Article 81, §326 (a) and Rule 70, the method suggested by both the appellee and the *amicus curiae* is sound, and the proper mode of dealing with the situation. Article 81, §326 (a), calling for non-taxation of state contractors, creates a valid and permissible exemption (Article 15, Declaration of Rights. Cf. *Oursler v. Tawes*, 178 Md. 471, 485; 13 A. 2d 763; *John McShain v. Comptroller, supra; Comptroller v. Joseph F. Hughes, supra*). In addition to Article 81, §326 (a), Article 81, 326 (f) prohibits the taxing of "sales which are not within the taxing power of this State under the Constitution of the United States." Thus the Legislature has incorporated into the statute itself a federal constitutional standard.[4] That standard requires, as we pointed out above,

[3] The Rules and Regulations adopted by the Comptroller are authorized by Article 81, §305 (a).

[4] Cf. Martin v. State Tax Comm'r, supra; Tawes v. Aerial Products, 210 Md. 627, 124 A. 2d 805; Steiner Const. Co. v. Comptroller, 209 Md. 453, 121 A. 2d 838.

that there be no invidious discrimination between the treatment afforded federal and state contractors. Consequently, when the Legislature carried out its intention to exempt state contractors (§326 (a)), sales to federal contractors were no longer "within the taxing power of this State under the Constitution of the United States." It would seem that this construction will permit the whole of the legislative fiscal program (as it applies here) to stand as it was originally projected, and the result is amply warranted by the canons of construction commonly applied by this and other Courts. See *Dept. of Tide. Fisheries v. Sollers*, 201 Md. 603, 613, 95 A. 2d 306, wherein the Court said, "it is presumed that the Legislature intends to impart to each of its enactments a meaning that will render it operative and effective." We hold that the second paragraph of Rule 70, as quoted in footnote (1), is unconstitutional, null, and void insofar as it attempts to tax contractors under a lump-sum contract with the Federal Government. If Maryland desires to tax federal contractors, it may do so in the same manner as the Illinois Legislature did after its state exemption was declared invalid (see above), *i.e.*, change the law so as to tax state contractors also. Cf. Smith-Hurd Ann. Stats., Ch. 120, §441, as amended by Act of July 31, 1961, Illinois Laws, 1961, p. 2312, §1.

IV.

The cross-appellant, Pittsburgh, here disputes the validity of the assessment on rentals of floating equipment. In 1955, the Legislature amended the then §320 (d), now §324 (d), of Article 81.[5] Pittsburgh argues that the definition of

[5] The following is the language used as it appears in Ch. 332 of the Acts of 1955:

"320 (d) [now 324 (d)] 'Sale' and 'Selling' mean any transaction whereby title or possession, or both, of tangible personal property is or is to be transferred by any means whatsoever for a consideration *including rental, lease, or license to use, or royalty*, by a vendor to a *purchaser*, or any transaction whereby services subject to tax under Section 321 of this sub-title are rendered for consideration to any purchaser by any vendor. Such consideration may be either in the form of a price in money, rights or property, or by exchange or barter, and may

"sale" and "selling," by including "rental" within the "sub-definition of 'consideration,' was not intended to pervert the normal meaning of 'sale' or 'selling'." Further, and this is the nub of its contention here, it claims that the inclusion of the word "rental" in the statute was not intended to impose a tax on short-term rentals without options to purchase, but was done for the sole purpose of making clear that the sales tax applies to transactions which are *in actual fact sales*, although they are disguised, for various purposes, as rentals.[6]

Such a construction would be a strained one, and necessitate ignoring the plain meaning of the language employed in the statute and the purpose thereof expressed in its title. The title, *inter alia*, states that the Act is "to impose the [sales] tax on rentals and leases of certain tangible personal property; * * * [to impose] the tax on leases of motor vehicles; * * * and to repeal and re-enact with amendments [Section] * * * 368 (f) (2) * * * of Article 81 * * *, subtitle 'Maryland Use Tax' [which is complementary to the sales tax] * * * amending the definition of 'Purchase' to include lease and rentals." Cf. *Kimball-Tyler v. Baltimore City*, 214 Md. 86, 96, 133 A. 2d 433.

Although the phraseology of the first sentence of §324 (d) can, perhaps, be properly termed clumsy, and probably few, if any, English teachers would commend it, it, together with the title and the remainder of the section, we

be payable immediately, in the future, or by installments. NOTHING IN THIS SUB-SECTION SHALL APPLY TO THE RENTING OF TEXTILES, THE ESSENTIAL PART OF WHICH INCLUDES THE RECURRING SERVICE OF LAUNDERING OR CLEANING THEREOF, NOR THE RENTING OF MACHINES AND EQUIPMENT USED EXCLUSIVELY FOR AGRICULTURAL PURPOSES."

Explanation: Italics indicate new matter added to existing law. [[Brackets]] indicate matter stricken from existing law. CAPITALS indicate amendments to bill.

[6] Cf. Beckwith Machinery Co. v. Matthews, 190 Md. 182, 57 A. 2d 796; Alban Tractor Co. v. State Tax Commission, 219 Md. 503, 150 A. 2d 456.

think, makes it clear that the Legislature intended to include all kinds of rentals of tangible personal property (not expressly excluded) in the sales tax law. The phrase "including rental, lease or license to use, or royalty," does not merely modify the single word "consideration," which precedes it, as argued by Pittsburgh, but it goes back and is to be considered in conjunction with everything that has preceded it in the sentence. In other words, "sale" and "selling" mean any transaction whereby title or possession, or both, of tangible personal property is, or is to be, transferred by any means whatsoever for a consideration, and any such transaction shall include rental, lease or license to use, or royalty (on tangible personal property), by an owner to a transferee. This construction is additionally bolstered, we think, by the exclusionary provisions of the subsection, whereby "renting" of such textiles as diapers, towels, barbers' blouses, etc. (under certain conditions), and the "renting" of machines and equipment used exclusively for agricultural purposes are excluded from the Act. We hold that the trial court was correct is sustaining the assessment for rentals of tangible personal property.

ORDER AFFIRMED, THE COMPTROLLER TO PAY 6/7 OF THE COSTS, AND PITTSBURGH 1/7 THEREOF.